

U.S. DEPARTMENT OF LABOR

SECRETARY OF LABOR  
WASHINGTON, D.C.

DATE: July 31, 1995  
CASE NOS. 83-CTA-084  
          83-CTA-158  
          83-CTA-193\*  
          83-CTA-201\*  
          84-CTA-080\*  
          84-CTA-174  
          85-CTA-070  
          85-CTA-110  
          85-CTA-113\*  
          85-CTA-120 <sup>1/</sup>

IN THE MATTER OF

U.S. DEPARTMENT OF LABOR,

COMPLAINANT,

v.

CITY OF DETROIT, MICHIGAN,

RESPONDENT.

BEFORE: THE SECRETARY OF LABOR

FINAL DECISION AND ORDER

This case arises under the Comprehensive Employment and Training Act (CETA), 29 U.S.C. §§ 801-999 (Supp. V 1981),<sup>1/</sup> implementing regulations then applicable at 20 C.F.R. Parts 675-689 (1990) (CETA regulations), and 41 C.F.R. Part 29-70

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<sup>1/</sup> Although all of the several docket numbers herein have been adjudicated in a single proceeding, only those with an asterisk are subject to the current review before the Secretary of Labor.

(1984)(administrative requirements for Department of Labor grants to 'state and local governments). <sup>2/</sup>

#### BACKGROUND

The City of Detroit (City) operated a CETA public service employment program (PSE program) from July, 1977 through June, 1981. Under the PSE program, the City employed approximately 2,400 unemployed persons in twenty-nine City departments. These jobs spanned a wide range of clerical and professional fields, including garbage collectors, recreation workers, office personnel, uniformed police officers, fire fighters, and others. A Department of Labor audit resulted in various disallowances of administrative costs charged to the CETA program. The ten captioned cases were consolidated by the Office of Administrative Law Judges. Six of these cases involved direct costs. An agreement resolving those six cases was reached under which the City would pay the Department \$800,000, either as an offset against any monies owed to the City or as an additional amount owed by the City.

The remaining four cases involve administrative costs disallowed for lack of documentation and are the subject of this proceeding. Instead of challenging the costs disallowed by the Grant Officer in these cases, the City prepared and substituted indirect cost proposals and central service cost allocation plans

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<sup>2/</sup> CETA was repealed effective October 13, 1982 and was replaced by the Job Training Partnership Act, 29 U.S.C. §§ 1501-1791 (1988), but CETA administrative or judicial proceedings pending as of that date were not affected. 29 C.F.R. § 1591(e).

for fiscal years 1977-78, 1978-79, 1979-80, and 1980-81 in order to document and support the disallowed administrative costs. Because of the expected audit costs for reviewing more than one year, the expected availability of accounting and other records for the most recent year, and the similarity of the various indirect cost proposals, the parties agreed to litigate only the most recent proposal (fiscal year 1980-81) and apply the results of that audit proportionally to the other years.

On July 31, 1989, the Administrative Law Judge (ALJ) issued a Decision and Order (D. and O.) on the substantive issues involved in the indirect cost proposal. On September 27, 1990, the ALJ issued an Order sustaining the Grant Officer's motion for reconsideration, but denying the request for modification of the indirect cost proposal base established by the D. and O. On October 12, 1990, the ALJ issued his Final Order determining that the indirect costs allocable to the CETA grants for fiscal years 1977-81 totalled \$6,209,640, resulting in disallowed costs in the amount of \$2,591,483. The ALJ also ordered the City to pay the Department of Labor \$800,000 pursuant to the settlement of the other six cases.

The Secretary asserted jurisdiction on November 20, 1990. Both parties filed exceptions. This Final Decision and Order affirms the various rulings in the July 31, 1989 D. and O., except for the ruling on the proper base, which I have modified as set out below.

The City's indirect cost proposal is an integral part of the process for establishing costs charged to CETA grants. As summarized by the ALJ:

costs chargeable to federally supported programs consist of two basic categories - direct and indirect. Direct costs are those costs which can be specifically or readily identified with a particular cost objective. Indirect costs are costs that are incurred for a common or joint purpose and benefit more than one program, activity, organization or function. These costs, such as certain administrative salaries, building maintenance and utilities, are necessary for overall administration and implementation of programs, but cannot be directly assigned to a particular program. These costs must be distributed to all programs in proportion to the benefits received by that program. Indirect costs are normally charged to federal awards via an indirect cost rate. The computation of the indirect cost rate, supported by workpapers and other documentation is called an indirect cost proposal. A central service plan and indirect cost proposal are methodologies used by an entity (City of Detroit) to equitably distribute indirect costs to benefiting programs or activities within the entity. The overall objective of central service plans and indirect cost proposals is to distribute the indirect costs to all activities that consume resources in proportion to the amount of resources consumed by that activity. For example, if activity "A" consumes twice as much of the resources included in the indirect cost pool as activity "B", activity "A" should be allocated twice as much of the indirect costs as activity "B".

An indirect cost proposal consists of two functional components, the pool and the base. The pool is an accumulation of all of the indirect costs that are to be allocated and consists of indirect costs for services provided to more than one program or activity, e.g., payroll processing, voucher audit, and financial accounting. The base is an accumulation of certain direct costs used to determine the ratio by which the indirect costs in the pool are allocated to the cost objectives. The base is used to allocate the pool of the City's allowable indirect costs between CETA and non-CETA ultimate cost objectives, i.e., in proportion to the benefits derived.

In selecting an appropriate base, it is important to determine the purpose of the costs included in the pool since different programs or activities will utilize services to different degrees and the proportionality should be recognized in the base. A labor intensive program will utilize more payroll services than capital intensive programs. In a simple indirect cost proposal there are multiple functions in the pool and an appropriate base must be selected that reflects those differing functions such as salaries or total costs. Once computed, the rate is used to compute grantee indirect cost entitlement. The indirect cost rate is defined as follows:

$$\frac{\text{Pool}}{\text{Base}} \quad \text{Indirect Cost Rate}$$

To determine entitlement for a particular grant or program, the program's share of base is multiplied by the indirect cost rate:

$$\text{Rate} \times \text{Particular Programs' [sic] Share of Base} = \text{Entitlement}$$

The sum of all particular programs [sic] share of the base must be equal to the total base used in calculating the indirect cost rate.

D. and O. at 6-7.

This decision examines the ALJ's rulings on the indirect cost proposal through a discussion of the exceptions filed by the parties.

#### DISCUSSION

##### Burden of Proof

The City excepts to the ALJ's determination of the burden of proof. D. and O. at 8-10. Under the captioned "burden of proof" regulation at 20 C.F.R. § 676.90(b), "[t]he party requesting the hearing shall have the burden of establishing the facts and the

entitlement to the relief requested." The City's position is that:

[I]t need only disprove the reasons given in the Audit Report as adopted by the Grant Officer in order to prove "entitlement to the relief requested" [under 20 C.F.R. § 676.90(b)]: i.e., reversal of the Auditor's disallowances from the cost pool. The City takes exception to the ALJ's construction of the burden of proof which would, in effect, shift the burden to the City to disprove reasons for disallowance not put forth by the Grant Officer.

City's exceptions at 12.

The City's interpretation of 20 C.F.R. § 676.90(b) is inconsistent with the regulatory language, which does not state that the party requesting the hearing automatically prevails, as a matter of law, if the precise reason for the Grant Officer's disallowance is not adopted by the ALJ. The party requesting the hearing must demonstrate that the disputed costs are lawful.

*Gordon v. Kane County CETA, Illinois*, Case Nos. 81-CETA-224, 81-CETA-311, Sec. Dec., Sept. 23, 1992, slip op. at 6-7; *Oro Development Corp. v. U.S. Dept. of Labor*, Case No. 86-JTP-6 (arising under CETA and the Job Training Partnership Act (JTPA)), Sec. Dec., Feb. 18, 1988, slip op. at 4-6; *In the Matter of City of Camden, New Jersey and Mark DelGrande*, Case No. 79-CETA-102, Sec. Dec., Oct. 16, 1986, slip op. at 14-19, *aff'd sub. nom. City of Camden, New Jersey v. U.S. Dept. of Labor*, 831 F.2d 449 (3d Cir. 1987). See *Omaha Tribe of Nebraska v. U.S. Dept. of Labor*, 998 F.2d 581, 583 (8th Cir. 1993).

Administering Agency for the CETA Program

The City excepts to the ALJ's ruling that its Employment and Training Administration was the administering agency for its CETA program, rather than the City as a whole through the various agencies employing CETA PSE participants. The ALJ found, in part, that:

The CETA regulations, which incorporate (Federal Management Circular] FMC 74-4, distinguish between the recipient of a grant and the grantee of the fund. 20 C.F.R. § 676.40-1 and 41 C.F.R. § 29-70.103. They identify the "recipient" of the grant as the prime sponsor, which is inter alia, a State or local government. 20 C.F.R. § 675.4(a) and (b); 41 C.F.R. § 29-70.102(b) and (c). However, FMC 74-4 identifies the grantee of the CETA funds as the "department or agency of State of (sic] local government which is responsible for administration of the grant." 41 C.F.R. § 29-70.102(a); FMC 74-4 Attach. A § B(8). By incorporating the provisions of FMC 74-4 into the CETA regulations, the Secretary expressed his intent that the two sets of regulations be read together as a whole. The CETA regulations implemented the general provisions of the Act which made funds payable to prime sponsors subject to regulation by the Secretary. 29 U.S.C. § 815. The specific procedures for prime sponsors to determine costs of CETA grants and other federally-aided programs were established by FMC 74-4. OASC-10 p.iii. Therefore, the regulations read as a whole intended for the prime sponsors to identify one agency to actually receive and administer CETA grant-funds. The dictates of reason make this system more' appropriate than the system argued for by the City.

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The fact that all 29 agencies [other than the Employment and Training Department] are not CETA grantees does not preclude the City from claiming indirect costs from each of the 29 agencies. The regulations provide that the prime sponsor may recover the indirect costs incurred in the administration of the CETA grant by agencies other than the Employment and Training Agency. 20 C.F.R. § 676.41-1(f); OASC-10 p. 2; FMC 74-4 Attach. A § F. Generally, the indirect costs that are recoverable are those incurred by other departments in supplying goods, services, and

facilities to the grantee department. FMC 74-4 Attach. A §§ F(1) and G(1). Indirect costs may include only those costs which are administrative and necessary to effectively operate the program. 20 C.F.R. § 676.41-1(f). Administrative costs, however, encompass a broad range of costs including:

salaries and fringe benefits of personnel engaged in executive, fiscal, personnel, legal, audit, procurement, data processing, communications, maintenance, and similar functions; related materials, supplies, equipment, office space costs, and staff training. 20 C.F.R. § 676.41-1(f)(1).

FMC 74-4 Attach. A § G(1) defines indirect costs allowable to other agencies more narrowly as "supporting costs." In order for the prime sponsor to recover the indirect costs of these other agencies, those costs must meet the requirements of allowability spelled out in the regulations.

D. and 0. at 10-12.

The City agrees with the ALJ's finding that it is entitled to indirect costs incurred in all 29 agencies in addition to the Employment and Training Department. However, the City excepts that the ALJ's determination that the City was not the grantee directly impacts upon the allowability of costs in Categories C and D (Cost Centers Which Are For Head Of Agency, and Salaries and Fringe Benefits For Head of Agency). This determination also, according to the City, indirectly impacts upon the ALJ's disallowance of costs in Categories A and B (Cost Centers That Function As A General Responsibility of Government, and Salaries and Fringe Benefits Which Are A General Responsibility Of Government). City's exceptions at 16. <sup>3/</sup>

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<sup>3/</sup> The costs disallowed by the Grant Officer in the following topical categories were costs that the auditor recommended should  
(continued...)

I concur in the ALJ's analysis of the applicable CETA regulations and federal cost principles to the effect that the City's Employment and Training Department was the administering agency for the CETA grants. The review of the pertinent provisions is consistent with judicial analyses for statutory construction. *Brown v. Gardner*, 115 S.Ct. 552, 554-56 (1994); *Dole v. United Steelworkers of America*, 494 U.S. 26, 35-42 (1990); *TVA v. Hill*, 437 U.S. 153, 172-73, 184-93 (1978).

41 C.F.R. § 29-70.103(a) provides that the cost principles in Federal Management Circular (FMC) 74-4 are applicable to the determination of allowable costs under Department of Labor grants with State and local governments. These cost principles are made

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<sup>3/</sup>( . ..continued)

be eliminated from the indirect cost pool in the City's Indirect Cost Proposal:

- Category A: Cost Centers That Function As A General Responsibility of Government.
- Category B: Salaries and Fringe Benefits Which Are A General Responsibility of Government.
- Category C: Cost Centers Which Are For Head of Agency.
- Category D: Salaries and Fringe Benefits For Head of Agency.
- Category E: Agencies in the Indirect Cost Proposal that Should be in the Central Staff Service Allocation.
- Category F: Capital Expenditures.
- Category G: Non-Personal Service Costs Not Supportive of CETA.
- Category H: Non-Personal Service Costs Associated with Unallowable Salaries.
- Category I: Non-Personal Service Costs Charged Only to Indirect Cost Pool.
- Category J: Revenues Allocable to Administering CETA.

The parties and the ALJ followed these topical headings as listed in the audit of the Indirect Cost Proposal. D. and O. at 8.

specifically applicable to CETA grants through 20 C.F.R. § 676.31(b) and 41 C.F.R. § 29-70.101(f)(3). FMC 74-4, Attach. A, § B(8) , defines a grantee as "the department or agency of a State or local government which is responsible for the administration of the grant." I agree with the Grant Officer that if the costs charged to the CETA grant are administrative, the agency charging these costs must be the agency responsible for the administration of the CETA program, in this case the City's Employment and Training Department, rather than each City PSE employing agency.

That PSE employing agencies may have supervised CETA participants is not a reasonable or sound basis for concluding that they were all administering the CETA grant. The Employment and Training Department was "the department ... of [the) . . . local government ... responsible for the administration of the grant" under FMC 74-4, Attach. A, § (B)(8), because administrative costs and activities are "associated with the management of the program." 20 C.F.R. § 676.41-1(f). That department was responsible for typical management, i.e. administrative functions, "including the responsibility for determining participant eligibility, for funding the PSE positions, for being accountable to the Department of Labor for the CETA funds, for CETA budgeting, and for monitoring and submitting reports to the Department of Labor." Grant Officer's brief at 36-37. The Grant Officer's interpretation is reasonable and should be accorded deference as the interpretation of the

agency charged with implementation and enforcement of the statute and'pertinent regulations. *Chicano Education and Manpower Services v. U.S. Dept. of Labor*, 909 F.2d 1320, 1325 (9th Cir. 1990); *Blackfeet Tribe v. U.S. Dept. of Labor*, 808 F.2d 1355, 1357 (9th Cir. 1987). See *Board of Governors, Federal Reserve System v. Dimension Financial Corp.*, 474 U.S. 361, 368, 373 (1986); *Chemical Manufacturers Assn. v. Natural Resources Defense Council, Inc.*, 470 U.S. 116, 125 (1985).

Category A: Cost Centers That Function  
as a General Responsibility of Government

The City excepts to the ALJ's disallowances of Category A costs, Cost Centers That Function As A General Responsibility of Government, <sup>4/</sup> from the indirect cost pool in the City's Indirect Cost Proposal in the amount of \$17,989,635. The ALJ upheld the Grant Officer's Category A disallowances because: (1) the City had not demonstrated that these cost centers provided administrative or supporting services to the CETA program under 20 C.F.R. § 676.41-1(f)(1) and FMC 74-4, Attach. A § G(1), D. and O. at 13-14; (2) the City had not demonstrated that the costs were expended for the benefit of CETA and not to provide traditional public services, D. and O. at 16-17; and (3) assuming that the City established that the costs were administrative, it

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<sup>4/</sup> Category A costs involved twelve City agencies other than the Employment and Training Department: Civic Center (\$198,371), Consumer Affairs (\$184,000), Department of Public Works (\$745,426), Fire Department (\$6,676,110), Hospital (\$2,962,867), Mayor's Office (\$392,064), Public Information (\$685,000), Public Lighting (\$4,296,145) Recreation (\$1,495,265), Senior Citizens (\$264,620), and Election Commission (\$89,759). D. and O. at 12-13.

had not shown that they were necessary for the administration of CETA. D. and O. at 18.

I disagree with the City's position, City's reply brief at 18-19, that the costs fall within the definition of indirect administrative costs in 20 C.F.R. § 676.41-1(f)(1). The City views that section as broader than the definition given to supporting services in FMC 74-4, Attach A § B(12). Therefore, the City's position is that 20 C.F.R. § 676.41-1(f)(1) takes precedence over FMC 74-4, Attach. A § B(12) by reason of 20 C.F.R. § 676.40-1(a), which states that cost principles in the CETA regulations should be applied over conflicting federal cost principles. I agree with the ALJ that:

FMC 74-4 ... allow[s] *recovery* of indirect costs from other agencies only to the extent that they are "supporting costs." FMC 74-4 Attach. A § G(1). The definition of "supporting costs" is consistent with the CETA definition of administrative costs. Therefore, the regulations establish that indirect costs of other agencies may be recovered from CETA only if they are administrative costs.

D. and O. at 13; 20 C.F.R. § 676.31(b); 41 C.F.R. § 29-70.101(f)(3); *Florida Farmworkers Council, Inc. v. Marshall*, 710 F.2d 721, 727-28 (11th Cir. 1983).

In any event, indirect CETA administrative costs "must be necessary and reasonable for proper and efficient administration of the program," 20 C.F.R. § 676.40(a), and "shall be limited to those necessary to effectively operate the program." 20 C.F.R. § 676.41-1(f). Under these standards, I agree with the ALJ that the City "presented no evidence to explain how or why the claimed indirect costs from the named agencies were administrative or

supporting of its CETA grants." D. and O. at 14. <sup>5/</sup> Instead, the City offered broad allegations and conclusions. City's exceptions at 29-63; City's reply brief at 21-23. See Grant Officer's brief at 41-42. The City's expert witness had no experience in CETA cost matters. T. at 161-63, 402-03. The City was not excused from demonstrating under 20 C.F.R. § 676.90(b), that a cost benefits the CETA program if it is claimed as an indirect administrative cost, rather than a direct administrative cost. *Alameda County Training and Employment Board v. Donovan*, 743 F.2d 1267, 1270 (9th Cir. 1984); *Florida Farmworkers Council, Inc. v. Marshall*, 710 F.2d at 728.

The City excepts to the ALJ's affirmance of disallowances prohibited under 20 C.F.R. § 676.40(a) as "general expense[s] required to carry out the overall responsibilities of the

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<sup>5/</sup> For example the City offered no documentation demonstrating how costs incurred by the Recreation Department for maintenance and park protection, or by the Hospital for patient billing, benefitted the administration of CETA program. The burden is on the City to produce records supporting the claimed costs:

Record keeping is at the heart of the federal oversight and evaluation provisions of CETA and its implementing regulations. Only by requiring documentation to support expenditures is the DOL able to verify that billions of federal grant dollars are spent for the purposes intended by Congress. Unless the burden of producing the required documentation is placed on recipients, federal grantees would be free to spend funds in whatever way they wished and obtain virtual immunity from wrongdoing by failing to keep required records. Neither CETA nor the regulations permit such anomalous results.

*Montgomery County, Maryland v. Dept. of Labor*, 757 F.2d 1510, 1513 (4th Cir. 1985); *Colorado Dept. of Labor and Employment v. U.S. Dept. of Labor*, 875 F.2d 791, 793-94 (10th Cir. 1989); 20 C.F.R. § 676.34; 41 C.F.R. § 29-70.207-2.

recipient." D. and O. at 17. The ALJ's interpretation of the term as "[i]ncluding everything: comprehensive" is reasonable and within the plain meaning aimed at preventing recovery of costs associated with providing traditional governmental services. D. and O. at 17.

The placement of CETA participants in various agencies did not mean that the purpose and function of these agencies suddenly changed, *ipso facto*, from the provision of public services to special training institutions or instrumentalities for the benefit of the CETA program. As the ALJ concluded, the City's justification reflected its erroneous view "that because CETA employees worked in each of the agencies the indirect cost of each agency is recoverable." D. and O. at 18. This view is inconsistent with CETA maintenance of effort provisions in Section 121(g) of CETA, 29 U.S.C. § 823(g), and 29 C.F.R. § 676.73, which required grantees to use CETA funds to supplement and not supplant other funds. *Milwaukee County, Wisconsin, v. Donovan*, 771 F.2d 983, 992-93 (7th Cir. 1985); *State of Maine v. U.S. Dept. of Labor*, 669 F.2d 827, 828 (1st Cir. 1982). The City produced no evidence to demonstrate compliance with maintenance of effort requirements. D. and O. at 14-17; *Montgomery County v. Dept. of Labor*, 757 F.2d at 1513; 20 C.F.R. §§ 676.34, 676.73(g), 676.90(b); 41 C.F.R. § 29-70.207-2.

Category B: Salaries and Fringe Benefits  
Which Are a General Responsibility of Government

The City excepts to the disallowance of Category B costs, Salaries and Fringe Benefits Which Are a General Responsibility

of Government. <sup>6/</sup> The ALJ upheld the Grant Officer's Category B disallowances from the indirect cost pool in the amount of \$52,820,777.

The ALJ affirmed the disallowances for the same reasons he affirmed Category A disallowances. The ALJ held that the City had the burden of persuasion that the costs were allowable CETA administrative costs, were not ordinary expenses of government, did not violate maintenance of effort provisions, and were necessary for the administration of the CETA program. The ALJ held that the City had not met these standards:

The City failed to put on any proof that the recipient of the claimed salaries and fringe benefits performed any service to benefit the CETA grants. Neither did the City show that these positions did not exist before CETA or would not have been created absent CETA. Therefore, the City again failed to satisfy its burden of proof.

D. and O. at 19. I agree with the ALJ's holding and rationale. See my discussion of Category A costs, *supra*, which also applies to Category B.

Employment of PSE participants is not alone sufficient to justify these costs. I agree with the Grant Officer that the costs lack a nexus to the CETA program. "The purpose for supervising, for example, firefighters is to ensure that the

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<sup>6/</sup> Category B involved salaries and fringe benefits for employees of nineteen City agencies: Airport, Civic Center, Public Works Department, Fire Department, Historical, Hospital, Law Department, Mayor's Office, Municipal Parking, Police Department, Public Lighting, Recreation, Transportation, Zoological Park, City Council, Election Commission, Zoning, Recorder's Court, Library. Admin. File #5, Audit Report, Exh. I-2.

citizens ... are protected. . .. The firefighting supervisor is 'not administering the CETA program . Moreover, the supervisory function is necessary even if there are no CETA PSE participants." Grant Officer's brief at 49.

Category c: Cost Centers Which are for  
Heads of Agencies

The City excepts to the ALJ's affirmance of the Grant Officer's disallowance of Category C costs, Cost Centers for Heads of Agencies. These include \$3,648,171 of costs for centers attributed to the heads of four agencies,<sup>1/</sup> their staffs and associated costs, including medical malpractice and general patient liability insurance. The ALJ upheld this disallowance because FMC 74-4, Attach. A § C(1), for costs incurred by agencies other than the grantee, excludes costs of "supervision of a general nature such as that provided by the head of a department and his staff assistants not directly involved in operations." I agree with the ALJ that this provision is applicable since the City is incorrect in arguing that each of the four agencies is a grantee of CETA funds. D. and O. at 20; see my discussion, *supra*, affirming the ALJ's holding that the City's Employment and Training Department was the sole grantee.

I agree with the Grant Officer that the heads of the Hospital and Police Department are not directly involved in providing administrative support services for the administration

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<sup>1/</sup> Department of Public Works (\$419,167); Hospital (\$1,964,712); Police (\$490,114); Transportation (\$774,178). Admin. File #5, Audit Report, Exh. I-3.

of the CETA grant. "It is not the function of the hospital or the police department to provide administrative support to the CETA program; rather, it is the purpose of the hospital to provide health care and the purpose of [the] police department to provide public safety." Grant Officer's brief at 50.

Accordingly, I also agree with the ALJ that the City had not demonstrated that the costs were necessary and reasonable for the administration of the grant. D. and O. at 21. <sup>8/</sup>

The City repeats its argument to the ALJ that some of the costs, such as malpractice insurance, employee parking and professional dues, did not involve this cost category. I agree with the ALJ that this argument is irrelevant. While [the City] may be right to the extent that these costs could also be eliminated under a different category, I do not accept [its] argument that these costs are allowable. Not one of the costs . . . is an allowable cost to the CETA grant because they do not benefit any purpose of CETA." D. and O. at 21; 20 C.F.R.

§ 676.40. Moreover, as the Grant Officer correctly states:

It was the City, however, which classified these costs in this category. The auditor simply reviewed the cost centers developed by the City. The City can not now establish the allowability of some of these associated costs merely by reclassifying them. If the City can challenge the basis for the disallowances by reclassifying the costs, the City could simply change its books and charge all the indirect costs disallowed by the Grant Officer to cost categories other than the ones the auditor reviewed. It is the City's obligation

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<sup>8/</sup> The ALJ includes the requirements of 20 C.F.R. § 676.40, allowing costs necessary and reasonable for the proper and efficient administration of the CETA program, within his broad use of the term "maintenance of effort." D. and O. at 15.

to keep proper records and properly account for federal funds with adequate documentation to support the allowability of costs. 20 C.F.R. § 676.34; 41 C.F.R. § 29-70.207-2. The City still has the burden of demonstrating that the costs are allowable administrative costs which are reasonable and necessary for the proper and efficient administration of CETA, which the ALJ determined the City has not done.

Grant Officer's brief at 51.

Category D: Salaries and Fringe Benefits  
for Heads of Agencies

The City excepts to the ALJ's affirmance of the Grant Officer's disallowance of Category D costs, Salaries and Fringe Benefits for Heads of Agencies, from the indirect cost pool. These include \$1,918,887 of salaries and fringe benefits for the department heads of 14 City agencies. <sup>9/</sup> D. and O. at 21.

I agree with the ALJ's affirmance of this disallowance, which incorporated by reference his analysis and rationale for Category costs. D. and O. at 21. As discussed *supra*, I decline to accept the City's argument for allowability predicated upon its erroneous theory that all agencies with CETA PSE participants were grantees. The ALJ correctly held that the City did not meet its burden of proof. D. and O. at 21.

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<sup>9/</sup> Airport (\$54,528); Building and Safety Engineering (\$142,179); Civic Center (\$152,678); Fire Department (\$294,782); Historical (\$120,313); Law (\$141, 738); Municipal Parking (\$128,028); Public Lighting (\$177,345); Recreation (\$186,331); Zoological Park (\$122,709); Election Commission (\$53,011); Zoning (\$48,387); Recorder's Court (\$123,147); Library (\$173,711). Admin. file #5, Audit Report, Exh. I-4.

Cateaorv E: Agencies in the Indirect Cost Pool that  
Should be in the Central Service Allocation Plan

The City excepts to the ALJ's affirmance of the Grant Officer's elimination of \$8,503,000 <sup>10/</sup> from the indirect cost pool. The ALJ agreed with the Grant Officer that the costs should have been disallowed because they were included in the Central Service Cost Allocation Plan, or should have been included in the Plan, or were costs of the central budget agency. A central service cost allocation plan is the prescribed methodology for allocating costs incurred by central service agencies, such as data processing, personnel and finance, to agencies which benefit from these central services. The central service plan allocates these costs based on the extent to which the particular agencies use the services. OASC-10, Cost Principles and Procedures For Establishing Cost Allocation Plans And Indirect Cost Rates For Grants And Contracts With The Federal Government, at 6 (brochure containing FMC 74-4, cost principles applicable to grants and contracts with State and local governments, with related information and guidelines).

I affirm the ALJ's holding that central service costs 'disallowed by the auditor because they should have been included in the central service cost allocation plan but were not, are not recoverable by the City." D. and O. at 22. The ALJ's holding is correct since a grantee can claim only the central service costs

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<sup>10/</sup> Budget (\$1,152,000); Data Processing (\$556,000); Finance (\$3,024,000); Human Rights (\$315,000); Personnel (\$3,275,000); Auditor General (\$181,00). Admin. File #5, Audit Report, Exh. I-5.

which it has included as part of its central service cost allocation plan. Page 3 of OASC-10 specifically states that "it is necessary that the plans reflect all costs for which a claim is to be made." See *id.* at 6, 20.

The ALJ was correct in rejecting costs from the Indirect Cost Pool if they have been claimed in the Central Service Cost Allocation Plan since "[t]his would result in double billing." D. and O. at 22. Therefore, it was correct to eliminate Personnel Department costs already included in the Central Service Cost Allocation Plan. Admin. File #5, Audit Report, Exh. B-1. See 41 C.F.R. § 29-70.103.

The ALJ correctly affirmed the disallowance of costs of the Budget Agency from the indirect cost pool since the City had not demonstrated that agency employees participated in the budget process for the City's Employment and Training Department. D. and O. at 22-23. The City did not establish that its Budget Agency employees "actively participat[ed] in the grantee agency's [Employment and Training Department's] budget process," as required by the special exception in FMC 74-4, Attach. B § B(6) to the general rule that "[c]osts for services of a central budget office are generally not allowable since these are costs of general government." The City's argument that the costs should be allowed as costs for "the general management and support of CETA participants in the Budget Department which enabled the accomplishment of the CETA program," City's exceptions at 89, reflects the City's erroneous view that all

City agencies employing PSE participants are per se CETA administrative agencies.

Category F: Capital Expenditures

The City excepts to the ALJ's affirmance of the Grant Officer's disallowances of depreciation costs for buildings and equipment from the indirect cost pool. Allowable depreciation costs must be reasonable and necessary for the proper and efficient administration of the CETA program, 20 C.F.R. §§ 676.40(a), 676.41-1(f); FMC 74-4, Attach A § C(1)(a), and must be documented through proper records, 20 C.F.R. §§ 676.34, 676.35; 41 C.F.R. § 29-70.207-2; FMC 74-4, Attach B § B(11)(c). I agree with the ALJ that the City did not provide documentation showing that the equipment or buildings had been used for the benefit of the CETA programs, or even documentation that identifies the property or equipment. Therefore, the City failed to carry its burden of proof establishing that the depreciation costs should be included in the indirect cost pool. D. and O. at 24.

The City argues that "[w]ithout the necessary equipment and appropriate office space, the CETA program objectives ... could not have been achieved. Obviously, the CETA program benefitted from equipment usage and office occupancy ...." City's exceptions at 94-95. As discussed *supra*, this argument reflects the City's erroneous view that the various City agencies employing PSE participants are all CETA grantees.

Catearv G: Non-Personal Service  
costs Not Supportive of CETA

The City excepts to the ALJ's affirmance of the Grant Officer's disallowance of \$7,496,388 in non-personal service costs from the indirect costs pool involving fourteen City agencies <sup>11/</sup> for such items as automotive repairs, towing and maintenance, building rentals, police uniforms, printing, advertising, fire and liability insurance, office supplies, and legal and travel expenditures. D. and O. at 24; Admin. File #5, Audit Report, Exh. 1-10. The ALJ held that the City did not show that these "costs were expended for proper and efficient administration of the CETA program and were expended strictly for the benefit of CETA." D. and O. at 25; see 20 C.F.R. §§ 676.40(a), 676.41-1(f).

The AU was correct in finding that:

The City did not present any evidence to explain how the disallowed expenses were strictly related to providing employment training services to the unemployed or under-employed citizens of Detroit. In reviewing the disallowed costs, not one cost was identified that was incurred strictly for administration of the CETA programs. For example, the cost of fire and liability insurance for the airport has no bearing upon employment training and is a cost the City bears absent CETA. The same is true for zoological park advertising, security guards at the library, book binding at the library, police towing costs, and the other costs disallowed under this category. In addition, I note that the costs of the mayor's office is [sic] not chargeable to CETA. FMC 74-4 Attach. B § C(6).

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<sup>11/</sup> The agencies and costs include: Airport (\$3,186); Building and Safety (\$33,938); Law (\$200,605); Mayor's Office (\$4,949); Municipal Parking (\$4,760,919); Zoological Park (\$49,812); Zoning (\$35,220); Recorder's Court (\$997,986); Library (\$155,820). Admin. File #5, Audit Report, Exh. 1-10.

. . . It is simply not reasonable to suggest that the City paid extra rent for courtroom space previously occupied because a CETA employee filled it while working as a court reporter or other employee of the court. Therefore, the recovery of that cost is precluded by the maintenance of effort regulations. 20 C.F.R. § 676.73.

D. and 0. at 24-25.

The City argues that much of the disallowed costs in Category G were costs for building space and equipment used for both administrative and operational purposes and that it was improper to disallow all of these costs since some of them were allowable as administrative costs. City's exceptions at 97; City's supplemental exceptions at 7. (Operational costs are not administrative costs and cannot be charged to the administrative cost category. 20 C.F.R. §§ 676.41, 676.41-1(f).) I agree with the Grant Officer that the City was obligated to account for and keep records to document the allowability of costs charged to the CETA grant. 20 C.F.R. §§ 676.34 and 676.35; 41 C.F.R. § 29-70.207-2. The City cannot expect or require that the Grant Officer perform the City's own record-keeping and documentary obligations to enable the City to justify and perfect these claims. *Mitchell v. EG & G (Idaho)*, Case No. 87-ERA-22, Sec. Dec., July 22, 1993, slip op. at 11-14.

Catesorv H: Non-Personal Service Costs  
Associated with Unallowable Salaries

The City excepts to the ALJ's affirmance of the Grant Officer's indirect cost pool disallowance of \$3,512,771 in non-personal service costs, such as rent and office supplies, associated with personnel whose salaries and fringe benefits had

been disallowed as not necessary and reasonable for the proper and efficient administration of CETA, 20 C.F.R. §§ 676.40(a) and 676.41-1(f). D. and O. at 25. I agree with the ALJ's holding that "[i]t is incumbent upon the City to maintain an accounting system that will document the costs charged to the grants. ... By its own admission, the City's accounting system cannot associate non-personal service costs with particular personnel." D. and O. at 25. As explained *supra*, the City was required to distinguish costs which can be attributed to services providing a benefit to the administration of CETA from costs which cannot be so distinguished or attributed. Only costs which can be associated with services providing a benefit to the administration of CETA can be included in the indirect cost pool.

Category I: Non-personal Service Costs  
Charged Only to the Indirect Cost Proposal

The City excepts to the ALJ's affirmance of the Grant Officer's disallowance of \$216,470 in non-personal service costs, such as office supplies, postage, telephone, printing and rent, for five City agencies (Building and Safety, Law, City Council, Recorder's Court, Library) since the City had not documented that these costs were necessary and reasonable for the proper and efficient administration of CETA. 20 C.F.R. §§ 676.40(a) and 676.41-1(f); D. and O. at 26; Admin. File #5, Audit Report, Exh. I-12. The auditor concluded that the City had "billed all office supplies, telephone, postage, printing, rentals and other similar charges entirely to the indirect cost pool," notwithstanding that "[t]hese charges are for administering and operating [each]

agency and, therefore should be allocated between the administration and operations of [each] agency." Exh. I-12. At the hearing, the City's witness admitted the correctness of the auditor's view that the City had not allocated these costs between administration and operations. T. at 257-59.

Accordingly, I agree with the ALJ that "[t]he City's expert did not attempt to justify the claimed costs or to explain why the costs were properly claimed .... [T]he City bears the burden of establishing the right to recover the claimed costs . . . [and] ... establishing an accounting system that will properly allocate its indirect costs to the CETA grant." D. and O. at 26. Therefore, I concur in the holding that the disallowances were proper in view of the City's failure to carry these burdens.

Catearv K: Costs Not Related to Administerina CETA

The City excepts to the ALJ's affirmance of the Grant Officer's decision to eliminate from the indirect cost pool \$17,905,454 in costs related to water, sewage and EPMD motor transportation (Public Works Department). The auditor — recommended that the costs for water and sewage and for EPMD motor transportation be disallowed because they were not administrative costs under CETA. <sup>12/</sup> I agree with the ALJ's

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<sup>12/</sup> Although the ALJ's affirmance of the disallowance was correct, his D. and O. is not especially clear as to the precise basis for the Grant Officer's disallowance. The auditor's objection was not that the City had included these costs in its Central Service Cost Allocation Plan, but rather that the City "rolled" these costs into the indirect cost proposal, notwithstanding that "[these] costs are not administrative costs (continued...)

affirmance of these water, sewage and motor transportation cost disallowances since the City did not demonstrate that these were proper CETA administrative costs, rather than overhead or operational costs for such purposes as filling swimming pools, watering parks, providing water for drinking and personal hygiene, and use allowance and maintenance of garbage trucks, fire engines, police cars and other vehicles. Such agency operating costs are not transformed into CETA administrative costs merely because CETA PSE participants may have been employed by these agencies or utilized particular items. Moreover, as the auditor noted, *id.* at I.42 - 1.43, these charges are costs that the City would incur regardless of the CETA program. Accordingly, charging them to CETA would be a violation of the maintenance of effort regulation at 20 C.F.R. § 676.73.

Emwlovment and Training Dewartment (Manpower Agency)

The City contends that the ALJ should have addressed Manpower Agency costs (Employment and Training Department) purportedly due the City through central service staff .

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<sup>12/</sup> (. . .continued)

per the CETA definition of administration and therefore should not be included in the Central Staff Service Allocation Plan which is rolled into the Indirect Cost Proposal. ... We have explained below the reasons for our determining that the costs were for operations instead of administration." Admin. File #5, Audit Report at I.41 (emphasis added). In other words, the auditor determined that the water and sewage costs and the EPMD motor transportation costs were not administrative costs reasonable and necessary for the administration of CETA. *Id.* at I.41 - 1.44.

allocations. I agree with the Grant Officer that this issue was not within the scope of the hearing, as follows:

The ALJ's Decision did not address the central service costs allocated to the Employment Training Department because it was not an issue before the ALJ. The auditor had determined that the central service cost allocation plan should result in the allocation of \$276,088 in central service costs to Employment and Training Department for fiscal year 1980. [sic] This was, in fact, \$147,629 more than the City had claimed in central service cost allocation plan it had submitted. [sic] (Adm. File No. 5, Audit 1.2). The City, obviously, accepted the auditor's finding.

The issue of what central service costs which were allocated to the Employment and Training Department for Fiscal Years 1977-1979 could be charged to CETA was not presented to the AU and no evidence regarding this issue is in the record. For all anyone knows the City could have already charged the CETA grant the central service costs allocated to the Employment and Training Department for Fiscal Years 1977-1979. If so, the City's attempt to claim these costs now would be double billing the grant. Since there is no evidence in the record, the City clearly has not demonstrated its entitlement to any additional central service costs.

The only issue[s] presented to the ALJ were issues relating to the indirect cost pool and base. These were the only issues resolved by the ALJ and, therefore, are the only issues before the Secretary. Any issues relating to the central service cost allocation plan submitted for Fiscal Year 1980 and central service cost allocations [for] Fiscal Years 1977 through 1979 have been waived.

In making this argument, the City relies heavily on the indirect cost negotiation agreement dated April 14, 1987 which the City has not signed. The Grant Officer finds it ironic that the City is relying on an indirect cost negotiation agreement which it has refused to sign. If the City wishes to rely on this document, the City ought to sign it. The Department is prepared to allow the City to claim the amounts of indirect costs provided in the agreement. If the City signs this indirect cost negotiation agreement, this case is moot. If the City chooses not to sign the agreement, this case is moot. If the City chooses not to sign the agreement, the City can not rely on some parts of the neatiated agreement and litigate others.

Grant Officer's brief at 78-80 (footnote omitted) (emphasis in original).

The record shows that this issue was not within the scope of these proceedings. Pretrial Conf. T. at 6-13; Hearing T. at 13-36; City's brief to the ALJ at 1-7, 75-76; City's reply brief to the ALJ at 1-4, 27-36. Issues not raised before the ALJ are "considered resolved and not subject to further review." 20 C.F.R. § 676.88(f).

#### The Indirect Cost Base

The Grant Officer excepts to the ALJ's holding that the indirect cost base utilized by the City, total direct salaries, wages, and fringe benefits, was the correct base. D. and O. at 30. <sup>13/</sup> The Grant Officer urges that the base against which the indirect cost pool is compared in determining the indirect cost rate should be total direct costs, including non-personnel costs, and that the costs that were improperly included in the indirect cost pool should be transferred to the base. As an alternative, the Grant Officer urges that if the base is not changed to total direct costs *i.e.* including non-personnel costs, I should enlarge the base approved by the ALJ to include the salaries, wages and fringe benefits that had been eliminated from the pool. I believe the latter approach is appropriate here.

I agree with the ALJ that as a general rule, a base of direct salaries, wages and fringe benefits is preferred. D. and

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<sup>13/</sup> This holding was reaffirmed in the ALJ's reconsideration order, Sept. 27, 1990, at 2.

0. at 29. Thus, OASC-10 at 12 states: "In most instances the types of costs allocated at the departmental level are most equitably allocated on a base of total direct salaries and wages or total direct salaries and wages plus applicable fringe benefits and, hence, these bases are preferred." Subject to my correction of the base to include the salaries, wages and fringe benefits that had been eliminated from the pool, I believe the ALJ's ruling is sound. While the quoted language in OASC-10 at 12 continues, "[h]owever, other bases, such as total direct costs less capital expenditures, may be used when they can be demonstrated to be more equitable," I agree with the ALJ that this language does not compel the use of a total direct costs base in this case because:

OASC-10 does not require the City to establish that its chosen base is more equitable than others unless it uses one other than direct salaries, wages and fringe benefits. The Grant Officer did not find that the base used by the City was not equitable. He found only that another base was more equitable. This finding is not sufficient to require application of another base when the City utilized the base of preference and established that it was equitable. The fact that another base results in less costs being charged to the CETA grant does not equate with greater equity. Under OASC-10, equity depends upon allocation of costs in proportion to benefits received, not the level of expenditure.

D. and 0. at 29. In any event, my corrective enlargement of the base to include the salaries, wages and fringe benefits that had been eliminated from the pool vitiates the Grant Officer's inequity contention since "the vast majority of costs disallowed

from the indirect cost pool were salaries and wages." Grant Officer's brief at 75. <sup>14/</sup>

All costs must be classified as either a direct cost or indirect cost. OASC-10 at 2, 8-9, 12, 19-20, 21-22, 33-34, 39, 57. The ALJ's decision creates a third category of costs, "disallowed indirect costs," D. and O. at 29, contrary to the cost classification system in OASC-10. Therefore, the failure to include in the base the salary and wage costs properly eliminated from the indirect cost pool is inconsistent with a central concept in OASC-10: "bases [should] produce an equitable result in consideration of relative benefits derived." *Id.* at 34. The vast majority of costs disallowed from the indirect cost pool were salaries and wages. Significant services in the pool included payroll services and personnel services. Since all employees of the City benefitted from these types of services, the disallowed salaries, wages and fringe benefits should be transferred to the base consistent with such equity considerations. *Id.* at 12, 34, 37, Exh. C, n.(b) at 57. . Excluding these salaries, wages and fringe benefits from the base would distort the cost of services to the activities benefitted. Grant Officer's brief at 75; Grant Officer's reply brief to the ALJ at 11-13.

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<sup>14/</sup> The guidelines are not rigid or absolutist. See OASC-10 at 11-12.

As applied to disallowed salaries, wages and fringe benefits, I support the following views of the Grant Officer:

Since the ALJ properly eliminated costs from the indirect cost pool as unallowable indirect costs to the CETA program, these costs must be classified as direct costs. Since the costs were not indirect costs of the CETA program, the costs were, in fact, direct costs of the city government and should have never been included in the indirect cost pool.

\* \* \* \* \*

. . . Any cost, including, for example, salaries, are an item of expense and must be considered a cost objective. FMC 74-4 Att. A § B.4. Since indirect costs must be allocated to cost objectives benefitting from the indirect costs, FMC 74-4 Att. A § F.1, indirect costs must be allocated to the salaries of City personnel. . . which the ALJ properly eliminated from the indirect cost pool. The allocation of indirect costs to the direct costs receiving benefits from the indirect costs is accomplished by including the direct costs, including those direct costs eliminated from the indirect cost pool, in the base. As noted in OASC-10 Ex. C note (b), "[a]lthough a cost may be unallowable [in the indirect cost pool] if it either generated or benefited [sic] from the indirect costs, it should be moved to the base ... and allocated its share of indirect costs."

Grant Officer's reply brief at 6-8 (quoted alterations in original final sentence).

#### Waiver of Repayment by the Secretary

Although not raised in the ALJ proceedings, the City now requests waiver of repayment pursuant to 29 U.S.C. § 816(d)(2), which provides:

(2) If the Secretary concludes that a public service employment program is being conducted in violation of . . . (various sections of the Act], or regulations promulgated pursuant to such sections, the Secretary shall, ... order the repayment of misspent funds from sources other than funds under this Act or other funds used in connection with programs funded under this Act (unless, in view of special circumstances as

demonstrated by the recipient, the Secretary determines that requiring repayment would not serve the purposes of attaining compliance with such sections), and order such other sanctions or corrective actions as are appropriate.

(emphasis added). This statutory provision must be read in tandem with 20 C.F.R. § 676.88(c), which was promulgated to implement this "special circumstances" statutory language. *Chicano Education and Manpower Services v. U.S. Dept. of Labor*, 909 F.2d at 1326.

20 C.F.R. § 676.88(c) outlines the conditions under which repayment may be excused:

(c) Allowability of certain questioned costs. In any case in which the Grant Officer determines that there is sufficient evidence that funds have been misspent, the Grant Officer shall disallow the costs, except that costs associated with ineligible participants and public service employment programs may be allowed when the Grant Officer finds:

(1) The activity was not fraudulent and the violation did not take place with the knowledge of the recipient or subrecipient; and

(2) Immediate action was taken to remove the ineligible participant; and

(3) Eligibility determination procedures, or other such management systems and mechanisms required in these regulations, were properly followed and monitored; and

(4) Immediate action was taken to remedy the problem causing the questioned activity or ineligibility; and

(5) The magnitude of questioned costs or activities is not substantial.

The City may have procedurally waived its opportunity to ask for an exercise of discretion to excuse repayment because it did not first present this request to the Grant Officer and the ALJ. <sup>15/</sup>

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<sup>15/</sup> The City did not follow the procedure outlined in 20 C.F.R. § 676.88(c), which contemplates that requests to excuse repayment  
(continued...)

Assuming, *arguendo*, that the City has not waived an adjudication of 'this issue, it has not "demonstrated," as required by 29 U.S.C. § 816(d)(2), that it has satisfied the regulatory criteria necessary to excuse repayment. <sup>16/</sup>

The City does not explain how its request is justified under 20 C.F.R. § 676.88(c). Instead, without any reference to this regulation, it merely states:

In the instant case, the City of Detroit reasonably relied upon its interpretation of the regulations in incurring millions of dollars in indirect expense to operate the CETA program. It would not serve the purpose of attaining compliance with any sections of the regulations to require repayment of monies already spent for the CETA program. Furthermore, the CETA program is no longer in operation. Therefore, the Secretary of Labor should exercise its [sic] equitable power to waive repayment of any amounts incurred by the City of Detroit which the Secretary finds were not properly charged to the CETA program.

City's supplemental exceptions at 13.

In any event, I agree with the Grant Officer that the City should not receive a waiver of repayment because it did not maintain financial and accounting systems which would adequately document the allowability of CETA administrative costs, as

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<sup>15/</sup> (. ..continued)

be made at the Grant Officer level. Further, in neglecting to ask the ALJ to consider this matter, the City may have waived any rights to raise this issue subsequently to the Secretary. See 20 C.F.R. §§ 676.88(f) and 676.90(f); *Chicano Education and Manpower Services*, 909 F.2d at 1327-28.

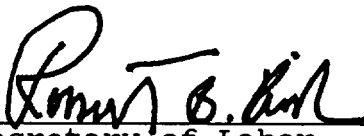
<sup>16/</sup> See *In the Matter of Worcester CETA Consortium*, Case No. 82-CETA-A-166, Sec. Dec., June 24, 1992; *U.S. Dept. of Labor v. City of Tacoma, Washington*, Case No. 83-CTA-288, Sec. Dec., June 26, 1991; *In the Matter of Louisiana Dept. of Labor*, Case No. 82-CPA-32, Sec. Dec., Aug. 23, 1990.

required under 20 C.F.R. § 676.88(c)(3), and the disallowed costs were substantial, contrary to 20 C.F.R. § 676.88(c)(5). Grant Officer's brief at 81. Accordingly, the City is not excused from repayment to the Department of Labor. *Bennett v. New Jersey*, 470 U.S. 632, 645-46 (1985); *Bennett v. Kentucky Dept. of Education*, 470 U.S. 656, 663-65 (1985).

## ORDER

The ALJ's Final Order IS MODIFIED to the extent that the indirect costs allocable to CETA shall be consistent with this Final Decision and Order. The excess indirect costs disallowed pursuant to this order, plus the disallowed direct costs in the ALJ's Final Order, shall be paid to the Department of Labor from non-Federal funds.

SO ORDERED.

  
Secretary of Labor

Washington, D.C.

CERTIFICATE OF SERVICE

Case Name: U.S. Department of Labor v. City of Detroit,  
Michigan

Case No. : 83-CTA-084, 83-CTA-158, 83-CTA-193\*, 83-CTA-201\*,  
84-CTA-080\*, 84-CTA-174, 85-CTA-070, 85-CTA-110,  
85-CTA-113\*, 85-CTA-120

Document : Final Decision and Order

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